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SUBJECT: U.S.-TURKEY ENERGY WORKING GROUP: TURKEY RECOMMITTS
TO TRANSIT GAS TO EUROPE BUT NO SOLUTION ON AZERI GAS

REF: ANKARA 1641

Classified By: DCM Doug Silliman for reasons 1.4 (B) and (D)

11. (C) Summary. Special Envoy for Eurasian Energy C. Boyden Gray and Deputy Assistant Secretary Matt Bryza led the U.S. delegation to the first U.S.-Turkey Energy Working Group. A summary of Gray and Bryza's points on Caspian energy is below. Iraq energy issues reported septel.

-- Turkey must quickly resolve the impasse with Azerbaijan on Shah Deniz phase II volumes, allowing at least 6 BCM to go to Europe to convince Azerbaijan to develop the field. This would give Turkey 4 BCM, short of its 8 BCM target, but much better than no Azeri gas;

-- The U.S. can help meet Turkey's energy supply needs by supporting projects that generate electricity with sources other than gas, and support energy conservation;

-- Turkey and the U.S. should work together to encourage Turkmenistan to allow entry of Western companies to develop Turkmen oil and gas fields; and

12. (C) Summary continued. Turkish delegation leader and his MFA and Energy Ministry team made the following points:

-- Turkey's first priority is additional gas for domestic use but this is not inconsistent with Turkey's desire to be a transit country for Europe;

-- Turkey requested U.S. support for its bid to open the EU Energy Chapter as soon as possible; and

--To unlock Turkmen gas, Turkey supports the EU concept for a private/public partnership, nominally called the Caspian Development Company (CDC).

13. (SBU) The first meeting of the U.S.-Turkey Energy Working Group took place in Ankara on September 15. The U.S. delegation was led by Eurasian Energy C. Boyden Gray and Deputy Assistant Secretary Matt Bryza. The Turkish side was led by MFA Deputy Undersecretary for Economic Affairs Selim Kuneralp and included MFA Deputy Director General for Energy, Water and Environmental Affairs Vural Altay, MFA Special Envoy for Iraq Murat Ozcelik Ministry of Energy Deputy Undersecretary Yusuf Yazar Turkish Petroleum General Manager Mehmet Uysal, BOTAS General Manager Saltuk Duzyol, Turkey's Nabucco Coordinator Osman Goksel, and other officials.

14. (C) MFA Deputy Undersecretary Kuneralp told Special Envoy Gray that the Russian invasion of Georgia had caught EU attention and highlighted the need for energy diversification for Europe sooner rather than later. For example, Hungarian Nabucco Coordinator Mihailly Bayer would visit Ankara later in the week and offer to host a Nabucco Summit in January. At the same time, Russia's invasion has complicated the investment picture by elevating the risks of the project. On balance, Kuneralp said South Stream was more likely suffer from Russian actions than Nabucco.

15. (C) Gray agreed that a "mental shift" had taken place in Europe which could help opening the route for gas westward. Similarly, the U.S. Administration was also now engaged in this issue at very high levels. DAS Bryza added the Russians did not attack the Baku-Tbilisi-Ceyhan (BTC) pipeline, although they did bomb railways to Supsa.

Turkey's Security of Supply -----

16. (C) Kuneralp explained the reasons for Turkey's demand for large volumes from Azerbaijan's Shah Deniz phase II (SD II) gas development. Turkey's electricity demand is growing by 6% a year, while gas demand is rising by 15%. Turkey is still working to expand its gas distribution network; 59 out of 71 provinces now have access to gas for residential and industrial use. Turkey's current annual gas consumption is

38 billion cubic meters (bcm). BOTAS General Manager Duzyol estimated that Turkey's demand will rise to 70 bcm by 2020. To meet this demand, Turkey will need to maximize volume intake from current contracts and also attract about 10 bcm in new supplies. These calculations assume Turkey will successfully renew existing contracts with Russia (for 6 bcm, expiring in 2011) and Algeria (4 bcm expiring in 2014). Without those contracts, the gap between supply and demand grows to 20 bcm.

17. (C) Ministry of Energy Deputy Undersecretary Yazar said Turkey has a strategy to reduce its dependence on natural gas. USD 125 billion in investment is needed by 2020 in order to raise the current installed electricity generation capacity (40,000 MW) to Turkey's goal of 80,000 MW. (Note: Most analysts believe the real installed capacity is about 27-28,000 MW because of obsolete machinery and inefficiencies.) Turkey aims to generate 25% of electricity with nuclear power by 2025. (Comment: This is unlikely. Bids for Turkey's first 4,000 MW nuclear plant are due September 24. Power is likely to come on-line around 2018-2020. End comment.) This tender represents 10% of Turkey's current generation or 5% of planned generation for 2020. Yazar also said that Turkey will be developing more generation from coal and renewable sources and has also launched a campaign on energy efficiency and conservation. In addition, Turkey would like to develop and transport Iranian and Iraqi gas.

Azerbaijani gas -----

18. (C) Kuneralp said meeting Turkey's internal energy demand is Turkey's first priority, followed closely by Turkey's strategic interest in becoming a transit state for Caspian and Iraqi gas to Europe. There is no inconsistency in this position; Turkey can do both but it must find adequate gas supplies. Gray said he understood Turkey's energy security needs but also cautioned that Turkey must both consume and transit Azeri gas from Shah Deniz II to make a deal work. Azerbaijan President Aliyev has repeatedly told the U.S. (and recently Vice President Cheney) that he wants to sell Azeri gas to Europe for strategic reasons. Gray said without an outlet to Europe, Azerbaijan will not develop the gas at all, and Turkey will receive no additional supply. 4-5 BCM is not

as much as Turkey needs, but it is much better than no gas. Turkey needs to look broadly at other sources to make up for the remaining 3-4 BCM, including new coal plants, electricity imports, LNG, renewables, and conservation. The U.S. is prepared to help Turkey develop these additional sources.

Turkmen gas

¶9. (C) Gray said the U.S. and Turkey need to work together with the EU and other allies to convey the same message to Turkmen leadership: "you must open up to foreign investors to bring new technologies and financing to the sector and to increase output." Turkish Nabucco Coordinator Goksel said a different approach is needed and suggested the creation of a private/public partnership, nominally called the Caspian Development Company (CDC) to bring technical skills, financing, and political support to the development of Turkmenistan's resources. Bryza expressed concern that CDC could crowd out or disadvantage private Western investors. Bryza said we should work together to draw up specific steps we can take together on Turkmenistan. Kuneralp agreed and the MFA will send us a draft.

Proposing alternatives - substitutes for natural gas

¶10. (C) Gray said we need to find new, inventive ways to help solve over-subscribed demand for SD II volumes. The U.S. wants to work with Turkey to reduce its gas usage by investing in other forms of electricity generation, such as coal-fired plants or renewables, and energy conservation. Gray said that the U.S. could help provide favorable financing terms through OPIC or Export-Import bank to make new energy deals feasible. Kuneralp was interested and suggested a more detailed discussion on the issue at a later date.

Where is the EU?

¶11. (C) Whether discussing Azeri, Turkmen or other gas sources, several GOT officials complained that the lack of a unified EU energy policy and changes in EU staff are complicating things for Turkey. Kuneralp said the EU Nabucco Coordinator would soon leave his position and EU Commissioner Piebalgs would take up the reigns beginning with a trip to the region, including Ankara in October. Kuneralp told Gray the EU wants Turkey to follow its rules and regulations for gas transmission but they refuse to open the Energy Chapter of the accession process, even though required benchmarks have been met. Gray said we view Turkey's accession process positively and that the U.S. will look for ways to encourage the EU to open Turkey's Energy Chapter.

¶12. (C) Bryza said he understood the EU was considering taking on some project risk for Nabucco through financing mechanisms of the European Investment Bank (EIB) or EBRD. Bryza said risk-sharing would improve investment climate for Nabucco and that the EU should announce this type of support right away.

Pipeline security

¶13. (C) Kuneralp said there is no evidence of sabotage in the August 5 explosion and fire on the BTC line in Turkey but the investigation is still ongoing. Kuneralp suggested BTC investors may have an axe to grind since they want to take over security of the line. MFA had a interagency meeting to recommend steps to improve BTC security, including hard covers for block valves. TPAO and Botas reps said that a one-star Jandarma general has been given the responsibility for pipeline security.

Other issues

¶14. (C) U.S. delegation also raised U.S. objections to and legal sanctions against Turkish investment in Iran and the Ambassador's request on behalf of GE to delay Turkey's bid deadline for the upcoming nuclear tender. Kuneralp confirmed what we have been hearing that a deal with Iran could take a decade or more and that the current Iranian offer to develop South Pars is not economical for TPAO.

¶15. (C) Bryza suggested the WG jointly develop three action plans, one each on Azeri gas, Turkmenistan-Azerbaijan inter-connection, and Iraqi gas (including a coordinated effort by the U.S. and Turkish embassies in Baghdad to convince the GOI to accelerate gas production and its potential export to Turkey and Europe). Kuneralp agreed, with Turkey holding the pen on initial drafts.

¶16. (U) This cable has been cleared by SE Gray and DAS Bryza.

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WILSON